

THE HONORABLE MARSHA J. PECHMAN

UNITED STATES DISTRICT COURT  
WESTERN DISTRICT OF WASHINGTON  
AT SEATTLE

IN RE WASHINGTON MUTUAL, INC.  
SECURITIES, DERIVATIVE & ERISA  
LITIGATION

No. 2:08-md-1919 MJP

IN RE WASHINGTON MUTUAL, INC.  
CALIFORNIA SECURITIES LITIGATION

This Document Relates to:

Lead Case No. C09-664 MJP

**OUTSIDE DIRECTOR DEFENDANTS'  
MOTION TO DISMISS THE  
CONSOLIDATED AMENDED  
COMPLAINT**

**[DD-07]**

**NOTE FOR MOTION CALENDAR:  
March 29, 2010**

**ORAL ARGUMENT REQUESTED**

**OUTSIDE DIRECTOR DEFENDANTS' MOTION TO  
DISMISS THE CONSOLIDATED AMENDED COMPLAINT  
(NO. C09-664MJP) [DD-07]**

LEGAL17701679.1

**Perkins Coie LLP**  
1201 Third Avenue, Suite 4800  
Seattle, WA 98101-3099  
Phone: 206.359.8000  
Fax: 206.359.9000

# **TABLE OF CONTENTS**

	<b><u>Page</u></b>
I. INTRODUCTION .....	1
II. THE ALLEGATIONS IN THE AMENDED COMPLAINT.....	3
III. PLAINTIFFS' ALLEGATIONS AGAINST THE OUTSIDE DIRECTOR DEFENDANTS FAIL TO SATISFY THE PLEADING REQUIREMENTS OF RULE 9(b) .....	6
A. Rule 9(b) Applies to All Claims Against the Outside Director Defendants .....	6
B. None of Plaintiffs' Claims Against the Outside Director Defendants Satisfies the Pleading Requirements of Rule 9(b) .....	7
IV. PLAINTIFFS FAIL ADEQUATELY TO ALLEGE RELIANCE.....	13
V. PLAINTIFFS' CALIFORNIA CORPORATIONS CODE CLAIMS SHOULD BE DISMISSED .....	14
A. The Outside Directors Are Not Alleged to Be Sellers .....	15
B. There is No Private Cause of Action Under Section 25403 .....	15
VI. CONCLUSION.....	16

**TABLE OF AUTHORITIES****Page****Cases**

<i>Apollo Capital Fund, LLC v. Roth Capital Partners, LLC</i> , 158 Cal. App. 4th 226, 70 Cal. Rptr. 3d 199 (2007).....	7, 15
<i>Atari Corp. v. Ernst &amp; Whinney</i> , 981 F.2d 1025 (9th Cir. 1992) .....	14
<i>Bains v. Moore</i> , 172 Cal. App. 4th 445, 91 Cal. Rptr. 3d 309 (2009) .....	11
<i>Cal. Amplifier, Inc. v. RLI Ins. Co.</i> , 94 Cal. App. 4th 102, 113 Cal. Rptr. 2d 915 (2001) .....	7, 14
<i>Casey v. U.S. Bank Nat. Ass'n</i> , 127 Cal. App. 4th 1138, 26 Cal. Rptr. 3d 401 (2005).....	12
<i>Diaz v. Federal Express Corp.</i> , 373 F. Supp. 2d 1034 (C.D. Cal. 2005) .....	7
<i>Haskin v. R.J. Reynolds Tobacco Co.</i> , 995 F. Supp. 1437 (M.D. Fla. 1998) .....	8
<i>In re Actimmune Marketing Litig.</i> , 614 F. Supp. 2d 1037 (N.D. Cal. 2009) .....	8
<i>In re GlenFed, Inc. Sec. Litig.</i> , 42 F.3d 1541 (9th Cir. 1994).....	8
<i>In re GlenFed, Inc. Sec. Litig.</i> , 60 F.3d 591 (9th Cir. 1995).....	9
<i>In re Hienergy Technologies, Inc.</i> , No. SACV04-1226 DOC, 2005 WL 3071250 (C.D. Cal. 2005).....	10
<i>In re Marsh &amp; McLennan Cos., Inc. Sec. Litig.</i> , 501 F. Supp. 2d 452 (S.D.N.Y. 2006).....	11
<i>In re Nat. Century Fin. Enters., Inc.</i> , 504 F. Supp. 2d 287 (S.D. Ohio 2007).....	9
<i>In re Ross Sys. Sec. Litig.</i> , No. C-94-0017-DLJ, 1994 WL 583114 (N.D. Cal. July 21, 1994) .....	12
<i>In re Silicon Storage Tech., Inc. Shareholder Deriv. Litig.</i> , No. C 06-3359 JF (RS), 2009 WL 1974535 (N.D. Cal. July 7, 2009).....	12
<i>In re Syntex Corp. Sec. Litig.</i> , 855 F. Supp. 1086 (N.D. Cal. 1994), <i>aff'd</i> , 95 F.3d 922 (9th Cir. 1996).....	9, 12
<i>In re Washington Mutual, Inc. Sec., Deriv. &amp; ERISA Litig.</i> , 259 F.R.D. 490 (W.D. Wash. 2009) .....	1, 8
<i>In re Washington Mutual, Inc. Sec., Deriv. &amp; ERISA Litig.</i> , Nos. 2:08-md-1919 MJP, C08-387 MJP, 2009 WL 3517630 (W.D. Wash. Oct. 27, 2009).....	2
<i>Kainos Labs., Inc. v. Beacon Diagnostics, Inc.</i> , No. C-97-4618 MHP, 1998 WL 2016634 (N.D. Cal. Sept. 14, 1998) .....	7, 9

**TABLE OF AUTHORITIES**  
(continued)

	<b><u>Page</u></b>
<i>Kamen v. Lindly</i> , 94 Cal. App. 4th 197, 114 Cal. Rptr. 2d 127 (2001) .....	9, 14, 15
<i>Kearns v. Ford Motor Co.</i> , 567 F.3d 1120 (9th Cir. 2009) .....	13
<i>Mirkin v. Wasserman</i> , 5 Cal.4th 1082, 23 Cal. Rptr. 2d 101 (1993) .....	13, 14
<i>Moore v. Kayport Package Express, Inc.</i> , 885 F.2d 531 (9th Cir. 1989) .....	9
<i>Morfin v. Accredited Home Lenders, Inc.</i> , No. 09-CV-792-WQH-BLM, 2010 WL 391838 (S.D. Cal. Jan. 26, 2010).....	9
<i>Murphy v. BDO Seidman LLP</i> , 113 Cal. App. 4th 687, 6 Cal. Rptr. 3d 770 (2003) .....	15
<i>Nat'l Union Fire Ins. Co. of Pittsburgh v. Cambridge Integrated Servs. Group, Inc.</i> , 171 Cal. App. 4th 35, 89 Cal. Rptr. 3d 473 (2009).....	7, 13
<i>Neilson v. Union Bank of Cal., N.A.</i> , 290 F. Supp. 2d 1101 (C.D. Cal. 2003) .....	7
<i>Small v. Fritz Cos., Inc.</i> , 30 Cal.4th 167, 132 Cal. Rptr. 2d 490 (2003).....	14
<i>Stack v. Lobo</i> , 903 F. Supp. 1361 (N.D. Cal. 1995) .....	10, 12
<i>Sunnyside Development Co., LLC v. Opsys Ltd.</i> , No. C 05-0553 MHP, 2005 WL 1876106 (N.D. Cal. Aug. 8, 2005).....	11
<i>Swartz v. KPMG LLP</i> , 476 F.3d 756 (9th Cir. 2007) .....	8, 9, 10
<i>Thomas v. Hickman</i> , No. CV F 06-0215 AWI SMS, 2006 WL 2868967 (E.D. Cal. Oct. 6, 2006) .....	8
<i>Valencia v. Merck &amp; Co.</i> , No. 1:07-CV-003880WWGSA, 2009 WL 3365848 (E.D. Cal. Oct. 16, 2009) .....	13
<i>Vess v. Ciba-Geigy Corp. USA</i> , 317 F.3d 1097 (9th Cir. 2003) .....	8
<i>Wojtunik v. Kealy</i> , 394 F. Supp. 2d 1149 (D. Ariz. 2005).....	10
<b>Statutes</b>	
Cal. Corp. Code § 25400.....	2, 7, 14
Cal. Corp. Code § 25403.....	3, 15
Cal. Corp. Code § 25500.....	14, 15

**TABLE OF AUTHORITIES**  
(continued)

	<b><u>Page</u></b>
<b>Regulations and Rules</b>	
Fed. R. Civ. P. 8(a) .....	1, 2
Fed. R. Civ. P. 12(b)(6).....	2
Fed. R. Civ. P. 9(b) .....	passim

1 The non-management directors of Washington Mutual, Inc. ("WaMu") named as  
 2 defendants in this action, Stephen Frank, Thomas Leppert, Phillip Matthews, Michael Murphy,  
 3 William Reed, Jr. and Orin Smith (collectively, the "Outside Director Defendants"), respectfully  
 4 submit this memorandum of law in support of their motion to dismiss the Consolidated Amended  
 5 Complaint ("Amended Complaint" or "Am. Compl.") in *In re Washington Mutual, Inc.*  
 6 *California Securities Litigation*, No. 2:08-md-1919 MJP, Lead Case No. C09-664 MJP (the  
 7 "California Securities Litigation").

## 14 I. INTRODUCTION

15 The allegations of fact in the Amended Complaint in the California Securities Litigation  
 16 are very similar—and in come cases identical—to the allegations in the extant complaint in *In re*  
 17 *Washington Mutual, Inc. Securities Litigation*, No. 2:08-md-1919 MJP, Lead Case No. C08-387  
 18 MJP (the "Federal Securities Litigation"). It is not surprising that tag-along plaintiffs in the  
 19 California Securities Litigation have adopted in wholesale fashion the allegations that this Court  
 20 has found to be sufficient to state certain federal securities claims against many of the same  
 21 defendants in the Federal Securities Litigation. However, in this case the charges against the  
 22 Outside Director Defendants are for California common law fraud and deceit, negligent  
 23 misrepresentation and violation of the California Corporations Code. These are not federal  
 24 securities claims, and this Court's prior assessment of the sufficiency of the allegations to support  
 25 federal securities claims is inapposite as applied to these fraud-based state law claims against the  
 26 Outside Director Defendants.

27 In the Federal Securities Litigation, the only primary claim against the Outside Director  
 28 Defendants is for violation of Section 11 of the Securities Act of 1933. Although the Outside  
 29 Director Defendants' motions to dismiss argued that the Section 11 claim sounded in fraud and  
 30 should be analyzed for compliance with the heightened pleading requirements of Federal Rule of  
 31 Civil Procedure ("Rule") 9(b), this Court concluded that the Section 11 allegations would be  
 32 tested by, and were sufficient under, the Rule 8(a) standard. *See In re Washington Mutual, Inc.*

1 *Sec., Deriv. & ERISA Litig.*, 259 F.R.D. 490, 503-04, 505 n.11 (W.D. Wash. 2009); *In re*  
 2 *Washington Mutual, Inc. Sec., Deriv. & ERISA Litig.*, Nos. 2:08-md-1919 MJP, C08-387 MJP,  
 3 2009 WL 3517630, at \*18 (W.D. Wash. Oct. 27, 2009). With respect to claims under the  
 4 Securities Exchange Act of 1934 against the Outside Director Defendants in the Federal  
 5 Securities Litigation, only Section 20(a) control person claims are asserted, and this Court held  
 6 that such claims, as well as control person claims under Section 15 of the Securities Act of 1933,  
 7 were sufficiently pled under the standards set by Rule 8(a). *Id.*

8  
 9 The Amended Complaint alleges causes of action against the Outside Director  
 10 Defendants for intentional fraud, negligent misrepresentation and violation of the California  
 11 Corporations Code, all of which are unquestionably fraud-based claims which must satisfy the  
 12 detailed pleading requirements of Rule 9(b) when brought in federal court. The claims against  
 13 the Outside Director Defendants in the Amended Complaint should be dismissed pursuant to  
 14 Rule 12(b)(6) because: (1) plaintiffs have failed to satisfy the requirements of Rule 9(b); (2)  
 15 plaintiffs have failed to satisfactorily plead justifiable reliance; and (3) the claims under the  
 16 California Corporations Code are not sufficiently plead or do not exist.

17  
 18 The Amended Complaint contains nothing more than general position-based allegations  
 19 against the Outside Director Defendants which offer no specificity as to these defendants as a  
 20 group, let alone each of the Outside Director Defendants individually. The Amended Complaint  
 21 therefore fails to plead its fraud-based claims against the Outside Director Defendants with the  
 22 particularity required by Rule 9(b) and should be dismissed. In addition, the Amended  
 23 Complaint fails to sufficiently plead the element of justifiable reliance as required for the  
 24 California common law claims of intentional fraud and negligent misrepresentation.

25  
 26 Finally, plaintiffs fail to state California statutory claims because the causes of action do  
 27 not apply to the Outside Director Defendants. Plaintiffs' claim under California Corporations  
 28 Code Section 25400 applies only to individuals who personally purchase or sell securities, and  
 29 plaintiffs do not allege that any of the Outside Director Defendants sold any WaMu securities

1 during the relevant time period. In addition, plaintiffs attempt to impose liability on the Outside  
 2 Director Defendants under California Corporations Code Section 25403, but there is no private  
 3 cause of action under that section.  
 4

## 5 6 7 **II. THE ALLEGATIONS IN THE AMENDED COMPLAINT**

8  
9 Plaintiffs Lou Solton, Treasurer of Monterey County, California (the "County"), and the  
 10 City of San Buenaventura (the "City") are or represent California public entities that allegedly  
 11 purchased WaMu notes and suffered damages as a result. Am. Compl. ¶¶ 60, 284, 312. On  
 12 July 11, 2007, the County "purchased a substantial interest in a WaMu note" with a May 1, 2009  
 13 maturity date. Am. Compl. ¶ 60. The City "purchased a substantial interest in a WaMu note,  
 14 with a maturity date on June 15, 2011." Am. Compl. ¶ 284. The Amended Complaint fails to  
 15 allege any details regarding plaintiffs' alleged purchases of these promissory notes. The  
 16 Amended Complaint contains no allegations regarding how plaintiffs purchased the promissory  
 17 notes, from whom, or for what amounts. Further, the Amended Complaint contains no  
 18 allegations that the Outside Director Defendants were sellers or were in any way involved in the  
 19 sale process. The County allegedly sold its note at a loss, although the Amended Complaint does  
 20 not disclose the date on which the County sold its interest in the note or the amount of the  
 21 alleged loss. Am. Compl. ¶¶ 60, 312. The City continues to hold the substantial interest in the  
 22 note it purchased and its investment has allegedly declined in value. Am. Compl. ¶ 312.  
 23

24  
25 On March 6, 2009, the County filed a complaint in California Superior Court alleging  
 26 causes of action for common law fraud and deceit, negligent misrepresentation, breach of  
 27 fiduciary duty and violations of the California Corporations Code. The action was removed to  
 28 the Northern District of California on April 3, 2009 pursuant to the District Court's original,  
 29 nonexclusive jurisdiction over civil proceedings related to Title 11 of the United States Code  
 30 under Section 1334(b) of the Judicial Code. *See* Am. Compl. ¶ 17. On April 17, 2009, the City  
 31 filed a virtually identical complaint in California Superior Court that was subsequently removed  
 32 to the Northern District of California on May 5, 2009. *See* Am. Compl. ¶ 17. On May 13, 2009,  
 33



1 the Judicial Panel on Multidistrict Litigation ordered both actions transferred to this Court for  
2 coordination with related pretrial proceedings already underway in this Court. Am. Compl. ¶ 18.

3  
4 Plaintiffs filed the Amended Complaint on January 4, 2010. In addition to the Outside  
5 Director Defendants, the Amended Complaint names as defendants Kerry Killinger, Thomas  
6 Casey, Stephen Rotella, Ronald Cathcart, David Schneider (collectively, the "Officer  
7 Defendants") and WaMu's outside auditor, Deloitte & Touche, LLP. The Amended Complaint  
8 alleges causes of action for fraud and deceit, negligent misrepresentation and violations of the  
9 California Corporations Code.

10  
11 The Amended Complaint alleges that the City and the County purchased and held their  
12 interests in WaMu notes based on alleged misrepresentations made by the defendants. *E.g.*, Am.  
13 Compl. ¶¶ 355, 369. The allegations are almost identical to those in the Federal Securities  
14 Litigation and allege that the Officer Defendants made misrepresentations in oral and written  
15 statements during WaMu "Investor Days," *e.g.*, Am. Compl. ¶¶ 120, 126, 127, 131, 167, 175,  
16 176, 207; during WaMu earnings calls, *e.g.*, Am. Compl. ¶¶ 165, 169, 177, 180, 186; in WaMu  
17 press releases, *e.g.*, Am. Compl. ¶ 169; at WaMu shareholder meetings, *e.g.*, Am. Compl. ¶¶ 171,  
18 179; and at other investor conferences, *e.g.*, Am. Compl. ¶¶ 170, 172, 173, 174, 178, 188, 210.  
19 But there are no such allegations of specific oral or written misstatements attributed to the  
20 Outside Director Defendants. The only alleged connection between the Outside Director  
21 Defendants and the alleged misrepresentations is that these defendants (along with certain of the  
22 Officer Defendants) signed WaMu's publicly filed year-end Forms 10-K for 2005, 2006 and  
23 2007, which plaintiffs allege contained material misstatements and omissions. Am. Compl. ¶¶  
24 187, 193, 294.

25  
26 The Amended Complaint does not allege that the Outside Director Defendants played any  
27 role in the day-to-day management of WaMu, let alone were in any way involved in the  
28 preparation or issuance of WaMu's financial statements. *See* Am. Compl. ¶¶ 28-34. Instead, the  
29 Amended Complaint generally alleges that the Outside Director Defendants had access to

1 allegedly adverse, nonpublic information about WaMu's risk management activities and "acted to  
2 conceal this information, or recklessly authorized and approved the concealment of the same."

3 Am. Compl. ¶¶ 349, 364. However, there are no allegations regarding how they gained this  
4  
5 alleged knowledge or how or why they allegedly concealed this vague, non-specific information.  
6  
7

8  
9 Moreover, the Outside Director Defendants are not mentioned individually except in the  
10 section of the Amended Complaint identifying the parties and in one paragraph identifying each  
11 of the Outside Director Defendants as a member of either the Finance Committee or the Audit  
12 Committee of the Board of Directors. Am. Compl. ¶ 338. Otherwise, the Amended Complaint  
13 refers to the Outside Director Defendants collectively as signatories on certain of WaMu's SEC  
14 filings, Am. Compl. ¶¶ 187, 193, 294, and in a section generally describing the role of WaMu's  
15 Board of Directors and the Board's Finance and Audit Committees. Am. Compl. ¶¶ 338-344.  
16  
17

18 The remainder of the Amended Complaint alternates allegations against unspecified  
19 "Defendants," *e.g.*, Am. Compl. ¶¶ 116, 127, with specific allegations concerning the Officer  
20 Defendants, either individually or as a group, or Deloitte & Touche, LLP. *E.g.*, Am. Compl. ¶¶  
21 155, 174, 176, 334.  
22  
23

24 The Amended Complaint fails to allege that the Outside Director Defendants participated  
25 directly in the alleged misconduct giving rise to the alleged misrepresentations. Also absent  
26 from the Amended Complaint are any particularized allegations concerning the substance of  
27 meetings involving any of the Outside Director Defendants, materials that were presented to or  
28 reviewed by the Outside Director Defendants relating specifically to any of the allegations in the  
29 Amended Complaint, specific statements attributed to any of the Outside Director Defendants, or  
30 any specific allegations of the Outside Director Defendants' involvement in the day-to-day  
31 management of WaMu.  
32  
33

34 The Amended Complaint contains only two paragraphs that refer to the Outside Director  
35 Defendants' purported knowledge with any specificity. Paragraph 184 alleges that William  
36 Longbrake, WaMu's former Vice Chairman of Enterprise Risk Management, Executive Vice  
37  
38  
39  
40  
41  
42  
43  
44  
45  
46  
47  
48  
49  
50  
51

1 President and CFO, "repeatedly warned the Board (including Board Chairman Killinger) that the  
 2 housing market was becoming too risky and WaMu should limit its exposure." And the  
 3 Amended Complaint alleges that WaMu filed a Schedule 14A on April 3, 2008 stating that "our  
 4 entire board are and have been actively engaged in formulating and overseeing management's  
 5 implementation of risk management policies." Am. Compl. ¶ 344. But neither of these  
 6 allegations is sufficiently specific to establish the Outside Director Defendants' scienter, and in  
 7 any event, these allegations are not specifically tied to any of the alleged misstatements. Instead,  
 8 plaintiffs rely on conclusory, boilerplate allegations such as that the Outside Director Defendants  
 9 "knew that information released to the public and WaMu's continuing course of action with  
 10 regards to its finances and risk management activities were destructive and could only end in  
 11 disaster." Am. Compl. ¶¶ 349, 364. The Amended Complaint does not allege that any of the  
 12 Outside Director Defendants sold WaMu stock during the relevant time period, nor does it allege  
 13 any other motivation for any of the Outside Director Defendants to engage in fraud.

14 The factual allegations regarding the Outside Director Defendants constitute little more  
 15 than boilerplate descriptions of the role of directors generally and provide no facts—let alone  
 16 particularized facts—regarding any connection between the Outside Director Defendants—as a  
 17 group or individually—and the alleged fraud.

### 18 **III. PLAINTIFFS' ALLEGATIONS AGAINST THE OUTSIDE DIRECTOR** 19 **DEFENDANTS FAIL TO SATISFY THE PLEADING REQUIREMENTS OF RULE 9(b)**

#### 20 **A. Rule 9(b) Applies to All Claims Against the Outside Director Defendants**

21 The California common law claims asserted against the Outside Director Defendants are  
 22 for intentional fraud, Am. Compl. ¶¶ 345-59, and negligent misrepresentation, Am. Compl.  
 23 ¶¶ 360-72. Under California law, the elements of a fraud claim which plaintiffs must prove are  
 24 (a) misrepresentation (false representation, concealment, or nondisclosure); (b) knowledge of  
 25 falsity; (c) intent to defraud, i.e., to induce reliance; (d) justifiable reliance; and (e) resulting  
 26 damage. *Diaz v. Federal Express Corp.*, 373 F. Supp. 2d 1034, 1066-67 (C.D. Cal. 2005)

(internal quotation marks and citations omitted). The elements of a negligent misrepresentation claim under California law are: "(1) the misrepresentation of a past or existing material fact, (2) without reasonable ground for believing it to be true, (3) with intent to induce another's reliance on the fact misrepresented, (4) justifiable reliance on the misrepresentation, and (5) resulting damage." *Nat'l Union Fire Ins. Co. of Pittsburgh v. Cambridge Integrated Servs. Group, Inc.*, 171 Cal. App. 4th 35, 50, 89 Cal. Rptr. 3d 473 (2009) (quoting *Apollo Capital Fund, LLC v. Roth Capital Partners, LLC*, 158 Cal. App. 4th 226, 243, 70 Cal. Rptr. 3d 199 (2007)). Although these are state law claims, federal pleading rules apply when such claims are, as here, brought in federal court. *Neilson v. Union Bank of Cal., N.A.*, 290 F. Supp. 2d 1101, 1141 (C.D. Cal. 2003) ("It is well-established in the Ninth Circuit that both claims for fraud and negligent misrepresentation must meet Rule 9(b)'s particularity requirements."). In addition, in order to bring a private action for damages under California Corporations Code Section 25400, plaintiffs must allege, with particularity, that the Outside Director Defendants made a knowingly false statement with deliberate intent to manipulate the price of a security pursuant to Section 25500. *See Kainos Labs., Inc. v. Beacon Diagnostics, Inc.*, No. C-97-4618 MHP, 1998 WL 2016634, at \*13 (N.D. Cal. Sept. 14, 1998) (requiring California Corporations Code claim under Section 25500 to be pled with particularity pursuant to Rule 9(b)); *Cal. Amplifier, Inc. v. RLI Ins. Co.*, 94 Cal. App. 4th 102, 109-10, 113 Cal. Rptr. 2d 915 (2001).

Accordingly, the particularized pleading standards of Rule 9(b) apply to each of plaintiffs' three causes of action against the Outside Director Defendants.<sup>1</sup>

**B. None of Plaintiffs' Claims Against the Outside Director Defendants Satisfies the Pleading Requirements of Rule 9(b)**

Rule 9(b) requires that, "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." To satisfy Rule 9(b), a complaint must allege "the who, what, when, where and how of the misconduct charged." *Vess v. Ciba-*

<sup>1</sup> The fraud, negligent misrepresentation, and California Corporations Code Section 25400 claims are collectively referred to as the "fraud-based claims" in the remainder of this section.

1 *Geigy Corp. USA*, 317 F.3d 1097, 1106 (9th Cir. 2003) (internal quotation marks and citation  
 2 omitted). A plaintiff must also provide an "explanation as to why the statement or omission  
 3 complained of was false or misleading." *In re GlenFed, Inc. Sec. Litig.*, 42 F.3d 1541, 1548 (9th  
 4 Cir. 1994). Although Rule 9(b) states that "motive, intent, knowledge, and other condition of  
 5 mind of a person may be averred generally," nothing in the Federal Rules of Civil Procedure  
 6 relieves plaintiffs of their obligation to plead facts from which an inference of scienter may be  
 7 drawn. *In re Actimmune Marketing Litig.*, 614 F. Supp. 2d 1037, 1048 (N.D. Cal. 2009). *See*  
 8 *Thomas v. Hickman*, No. CV F 06-0215 AWI SMS, 2006 WL 2868967, \*33 (E.D. Cal. Oct. 6,  
 9 2006) (dismissing fraud and negligent misrepresentation claims for failure to specifically allege  
 10 reason why defendant knew or should have known the alleged misstatement was false). This  
 11 Court's previous determination that the same or similar allegations were sufficient to support  
 12 non-fraud based claims against the Outside Director Defendants under Rule 8(a) in the Federal  
 13 Securities Litigation is inapplicable to the analysis of whether the Amended Complaint's  
 14 allegations satisfy the heightened pleading standards of Rule 9(b). *See In re Washington Mutual,*  
 15 *Inc. Sec., Deriv. & ERISA Litig.*, 259 F.R.D. 490, 504 (W. D. Wash. 2009). Plaintiffs must  
 16 satisfy Rule 9(b) with respect to each element of the fraud-based claims against the Outside  
 17 Director Defendants, and the allegations in the Amended Complaint fail to do so.

18  
 19 Plaintiffs do not even attempt to distinguish one director from another as required to  
 20 plead fraud with particularity under Rule 9(b). Plaintiffs' claims rest solely on allegations against  
 21 the Outside Director Defendants as a group or collectively as members of either the Board's  
 22 Audit Committee or Finance Committee. "Rule 9(b) does not allow a complaint to merely lump  
 23 multiple defendants together but 'require[s] plaintiffs to differentiate their allegations when suing  
 24 more than one defendant . . . and inform each defendant separately of the allegations surrounding  
 25 his alleged participation in the fraud.'" *Swartz v. KPMG LLP*, 476 F.3d 756, 764-65 (9th Cir.  
 26 2007) (quoting *Haskin v. R.J. Reynolds Tobacco Co.*, 995 F. Supp. 1437, 1439 (M.D. Fla.  
 27 1998)); *see also Morfin v. Accredited Home Lenders, Inc.*, No. 09-CV-792-WQH-BLM, 2010

1 WL 391838, at \*7 (S.D. Cal. Jan. 26, 2010). In the context of allegations of fraud against  
 2 multiple defendants, as here, a plaintiff must at a minimum "identif[y] the role of [each]  
 3 defendant[] in the alleged fraudulent scheme." *Swartz*, 476 F.3d at 765 (quoting *Moore v.*  
 4 *Kayport Package Express, Inc.*, 885 F.2d 531, 541 (9th Cir. 1989)). The Amended Complaint  
 5 fails to do so.  
 6  
 7  
 8  
 9

10 Although the Ninth Circuit has permitted plaintiffs to utilize the group pleading doctrine  
 11 as a means of satisfying Rule 9(b)'s particularity requirements, it is permissible against outside  
 12 directors only where a plaintiff can allege that "outside director[s] either participated in the day-  
 13 to-day corporate activities, or had a special relationship with the corporation, such as  
 14 participation in preparing or communicating group information at particular times." *In re*  
 15 *GlenFed, Inc. Sec. Litig.*, 60 F.3d 591, 593 (9th Cir. 1995); *see also Kainos Labs.*, 1998 WL  
 16 2016634, at \*13 (dismissing case against outside directors where plaintiffs made only conclusory  
 17 allegations regarding involvement of outside directors in corporate decision making); *Kamen v.*  
 18 *Lindly*, 94 Cal. App. 4th 197, 208, 114 Cal. Rptr. 2d 127 (2001) (refusing to apply group  
 19 pleading in statutory fraud case where plaintiffs failed to show that directors were involved in  
 20 day-to-day affairs of company or had special relationship with company). Here, plaintiffs fail to  
 21 allege any involvement by the Outside Director Defendants in WaMu's day-to-day management.  
 22 Plaintiffs do not allege any details of their involvement in underwriting, appraisals, risk  
 23 management or the preparation of financial statements. The Amended Complaint makes no  
 24 attempt to surmount the presumption that the Outside Director Defendants do not have day-to-  
 25 day involvement in WaMu's affairs. *See, e.g., In re Nat. Century Fin. Enters., Inc.*, 504  
 26 F. Supp. 2d 287, 297-98 (S.D. Ohio 2007) ("Outside directors, by contrast, cannot be assumed to  
 27 have assisted in preparing, reviewing, or approving offering materials."); *In re Syntex Corp. Sec.*  
 28 *Litig.*, 855 F. Supp. 1086, 1100 (N.D. Cal. 1994) ("By definition, outside directors do not  
 29 participate in the corporation's day-to-day affairs."), *aff'd*, 95 F.3d 922 (9th Cir. 1996). The  
 30  
 31  
 32  
 33  
 34  
 35  
 36  
 37  
 38  
 39  
 40  
 41  
 42  
 43  
 44  
 45  
 46  
 47  
 48  
 49  
 50  
 51



1 Amended Complaint therefore fails to plead particularized allegations against each of the  
 2  
 3 Outside Director Defendants pursuant to Rule 9(b).

4  
 5 The only allegation which attempts to connect the Outside Director Defendants to any  
 6  
 7 alleged misstatement is the Amended Complaint's assertion that the Outside Director Defendants  
 8  
 9 signed WaMu's Forms 10-K, Am. Compl. ¶¶ 187, 193, 294. But the bald allegation of the  
 10  
 11 Outside Director Defendants' signatures on documents which plaintiffs claim contain  
 12  
 13 misrepresentations is not enough to satisfy the particularity requirements of Rule 9(b) in the  
 14  
 15 absence of allegations specifically connecting each defendant to the underlying activity which  
 16  
 17 resulted in the alleged misrepresentation. *See Wojtunik v. Kealy*, 394 F. Supp. 2d 1149, 1165 (D.  
 18  
 19 Ariz. 2005); *Stack v. Lobo*, 903 F. Supp. 1361, 1376 (N.D. Cal. 1995) ("an outside director does  
 20  
 21 not become liable for the contents of a group published document merely by signing it"); *In re*  
 22  
 23 *Hienergy Technologies, Inc.*, No. SACV04-1226 DOC, 2005 WL 3071250, at \*6 (C.D. Cal. Oct.  
 24  
 25 25, 2005) (requiring plaintiffs to demonstrate scienter, in addition to a signature on public  
 26  
 27 document, in order to support fraud claim).

28  
 29 Nor can a plaintiff satisfy Rule 9(b) with vague and conclusory allegations that the  
 30  
 31 Outside Director Defendants knew about or participated in the wrongdoing. The Amended  
 32  
 33 Complaint includes numerous general allegations about "Defendants" followed by specific  
 34  
 35 alleged misrepresentations attributed to the Officer Defendants. *E.g.*, Am. Compl. ¶¶ 162, 164 *et*  
 36  
 37 *seq.* Allegations lumping the Outside Director Defendants with the other defendants without  
 38  
 39 providing any detail concerning the Outside Director Defendants fail to comply with Rule 9(b).  
 40  
 41 *Swartz*, 476 F.3d at 764-765 (dismissing fraud claims against Presidio and DB because  
 42  
 43 "[c]onclusory allegations that Presidio and DB 'knew that [other defendants] were making . . .  
 44  
 45 false statements to clients, including Swartz, and thus were acting in concert with [them]' and  
 46  
 47 'were acting as agents [of the other defendants]' and were 'active participants in the conspiracy'  
 48  
 49 without any stated factual basis are insufficient as a matter of law"). Vague allegations of  
 50  
 51 collusive fraud do not meet the requirements of Rule 9(b).

1 The few allegations regarding the Outside Director Defendants' alleged knowledge of  
 2 general business risk such as declining financial results amidst a nationwide housing market  
 3 collapse are insufficient to satisfy the requirement that plaintiffs plead fraud with specificity. For  
 4 example, the Amended Complaint alleges that Longbrake warned the Board that the housing  
 5 market was risky and that WaMu issued a statement asserting that WaMu's Board was actively  
 6 involved in risk management. Am. Compl. ¶¶ 184, 334. Such allegations say nothing about the  
 7 Outside Director Defendants' scienter. *See Sunnyside Development Co., LLC v. Opsys Ltd.*, No.  
 8 C 05-0553 MHP, 2005 WL 1876106, \*5 (N.D. Cal. Aug. 8, 2005) (dismissing allegations of  
 9 existence of "much evidence" supporting scienter as "conclusory," even taken in light most  
 10 favorable to plaintiff); *Bains v. Moore*, 172 Cal. App. 4th 445, 467-68, 91 Cal. Rptr. 3d  
 11 309 (2009) (finding that evidence that board knew about business challenges faced by company,  
 12 and that employee had emailed one board member with specifics, was insufficient to conclude  
 13 that board members knew of actual fraudulent activity carried out by employees). References to  
 14 generic risk factors or even a statement about general economic conditions provided to the  
 15 Outside Director Defendants do not satisfy Rule 9(b), particularly when they are not tied to any  
 16 specific alleged misstatement attributed to the defendants. Although the Amended Complaint  
 17 refers to various alleged "red flags," plaintiffs do not specifically connect any of those alleged  
 18 "red flags" to the Outside Director Defendants. *E.g.*, Am. Compl. ¶¶ 154 (Officer Defendants),  
 19 261 (Killinger), 333 (Deloitte). In any event, simply identifying "red flags," standing alone, has  
 20 no bearing on a defendant's scienter. *In re Marsh & McLennan Cos., Inc. Sec. Litig.*, 501 F.  
 21 Supp. 2d 452, 487 (S.D.N.Y. 2006) ("Merely labeling allegations as red flags, however, is  
 22 insufficient to make those allegations relevant to a defendant's scienter."). Plaintiffs have failed  
 23 to identify any specific information which was provided to the Outside Director Defendants  
 24 which would have alerted them to fraud, and plaintiffs do not connect any alleged knowledge on  
 25 the part of the Outside Director Defendants to any alleged misstatement.  
 26  
 27  
 28  
 29  
 30  
 31  
 32  
 33  
 34  
 35  
 36  
 37  
 38  
 39  
 40  
 41  
 42  
 43  
 44  
 45  
 46  
 47  
 48  
 49  
 50  
 51



Plaintiffs' allegations that the Outside Director Defendants participated in Board committees are also insufficient to satisfy Rule 9(b). *E.g.*, Am. Compl. ¶¶ 338, 341; *Stack*, 903 F. Supp. at 1376 (concluding that argument that directors were liable for group-published information because they were the sole members of company's audit committee is "unpersuasive"); *In re Syntex*, 855 F. Supp. at 1100 (concluding that allegations that an outside director chaired the corporate defendant's finance and trust revenue committees failed to establish the requisite involvement in the corporation's day-to-day affairs); *In re Ross Sys. Sec. Litig.*, No. C-94-0017-DLJ, 1994 WL 583114, at \*6 (N.D. Cal. July 21, 1994) (rejecting allegations that outside directors served on various board committees and signed SEC filings as insufficient to permit group pleading). Conclusory allegations about Board participation are insufficient to establish a reasonable basis to infer that the Outside Director Defendants knew about, let alone participated in, the issuance of any allegedly false statements. *See, e.g., In re Silicon Storage Tech., Inc. Shareholder Deriv. Litig.*, No. C 06-3359 JF (RS), 2009 WL 1974535, at \*11 (N.D. Cal. July 7, 2009) (rejecting allegations of committee membership as insufficient to establish directors' scienter in options backdating context).

The only alleged connection between the Outside Director Defendants and the alleged misrepresentations and omissions is that the Outside Director Defendants served as outside, independent directors of WaMu, served as members of various Board committees, signed certain of WaMu's publicly-filed documents and may have received generic information about economic conditions. These allegations fail to provide the detail required by Rule 9(b) to meet the elements of plaintiffs' fraud-based claims, and all of the claims against the Outside Director Defendants should therefore be dismissed.<sup>2</sup>

---

<sup>2</sup> Although the Amended Complaint contains no separate cause of action for aiding and abetting, plaintiffs claim that the Outside Director Defendants have been sued both "as participants and as aiders and abettors." Am. Compl. ¶ 47. This does not change plaintiffs' burden, as aiding and abetting liability requires "actual knowledge of the primary violation in which they purportedly participated." *Casey v. U.S. Bank Nat. Ass'n*, 127 Cal. App. 4th 1138, 1148, 26 Cal. Rptr. 3d 401 (2005). This burden is no lower than the burden for pleading direct liability for purposes of the fraud-based claims.

#### IV. PLAINTIFFS FAIL ADEQUATELY TO ALLEGE RELIANCE

Although the sufficiency of pleading standards for a complaint in federal court are governed by federal law, state law governs whether the pleaded elements state a cause of action. *Kearns v. Ford Motor Co.*, 567 F.3d 1120, 1126 (9th Cir. 2009). To state claims for fraud and negligent misrepresentation under California law, plaintiffs must allege justifiable reliance. *See supra* at 6-7.

California law requires that reliance be specifically pled by identifying how each plaintiff was exposed to the alleged misrepresentation and how the plaintiff relied upon the alleged misrepresentation to his or her detriment. *Mirkin v. Wasserman*, 5 Cal.4th 1082, 1099, 23 Cal. Rptr. 2d 101 (1993); *Valencia v. Merck & Co.*, No. 1:07-CV-003880WWGSA, 2009 WL 3365848, at \*8 (E.D. Cal. Oct. 16, 2009) (relying on *Mirkin* to reject allegation that plaintiffs "reasonably relied upon [information from defendants] in failing to take appropriate measures to protect themselves" as insufficiently specific); *Nat'l Union Fire Ins. Co. of Pittsburgh*, 171 Cal. App. 4th at 50 ("[T]here is a consensus that the causal elements [of negligent misrepresentation], particularly the allegations of reliance, must be specifically pleaded."). For purposes of pleading reliance under California law, it is not enough to plead that defendants made misrepresentations to the market with the intent that they be relied on. *Mirkin*, 5 Cal. 4th at 1099.

Plaintiffs do not even attempt to plead specific reliance on any statements by the Outside Director Defendants as required under California law. Indeed, the Amended Complaint does not allege plaintiffs' reliance on any statements directly connected to the Outside Director Defendants. Instead, the Amended Complaint repeatedly and broadly asserts that plaintiffs made purchases "in reliance on Defendants' misrepresentations and omissions." Am. Compl. ¶¶ 21, 60, 69, 280, 284. The fraud and negligent representation causes of action repeat a similar assertion that "Plaintiffs reasonably relied on these representations . . . in investing in and continuing to hold the WaMu notes and their reliance was justified." Am. Compl. ¶¶ 355, 369. Even if the allegations of reliance were connected to the Outside Director Defendants, plaintiffs

1 fail to allege any details to support their general assertion of reliance on "defendants"  
 2 misrepresentations and omissions. Mere assertion of reliance is inadequate. The failure to  
 3 adequately plead reliance requires dismissal of the fraud and negligent misrepresentation claims  
 4 against the Outside Director Defendants. *See Mirkin*, 5 Cal. 4th at 1086 (affirming dismissal for  
 5 failure to properly plead reliance with sufficient specificity).<sup>3</sup>

## 10 11 **V. PLAINTIFFS' CALIFORNIA CORPORATIONS CODE CLAIMS SHOULD BE** 12 **DISMISSED**

13  
 14 A violation of California Corporations Code Section 25400(d) requires (1) a statement  
 15 made by one who is selling, offering to sell, purchasing or offering to purchase a security; (2)  
 16 who has knowledge or reasonable ground to believe a statement is false or misleading; (3) which  
 17 statement is made for the purposes of inducing the purchase or sale of a security; and (4) made  
 18 with a specific intent to affect the price of a security. *See Cal. Amplifier, Inc.*, 94 Cal. App. 4th  
 19 at 110; *Kamen*, 94 Cal. App. 4th at 208 (2001). Enforcement of Section 25400 is limited to  
 20 administrative proceedings initiated by the California Department of Corporations. *Cal.*  
 21 *Amplifier, Inc.*, 94 Cal. App. 4th at 109. However, Section 25500 establishes a private right to  
 22 damages for violation of Section 25400 and imposes conditions for recovery that are not  
 23 included in Section 25400. *Id.* at 109, 111.<sup>4</sup> Most specifically, liability under Section 25500  
 24 requires an intent to defraud via a knowingly false statement. *Id.* at 112. In addition to the  
 25  
 26  
 27  
 28  
 29  
 30  
 31  
 32  
 33  
 34  
 35  
 36

---

37  
 38 <sup>3</sup> Although California recognizes a cause of action for holding a security based on misrepresentations, *see*  
 39 *Small v. Fritz Cos., Inc.*, 30 Cal.4th 167, 183-85, 132 Cal. Rptr. 2d 490 (2003), in order to proceed on such a cause  
 40 of action, a plaintiff must allege specific reliance on the defendants' representations, such as how and when it would  
 41 have sold the security if it had learned the new information. *Id.* at 183. Plaintiffs fail to satisfy this requirement, as  
 42 the Amended Complaint alleges only in boilerplate text that the City continued to hold its note in reliance on the  
 43 alleged misrepresentations. Am. Compl. ¶¶ 355, 369. Moreover, even if this boilerplate were sufficient to plead  
 44 reliance, plaintiffs cannot show that such continued reliance in holding their notes was justifiable. As they  
 45 characterize events in 2007, the "truth" was revealed when, on November 1, 2007, the New York Attorney General  
 46 allegedly filed a complaint against WaMu and several outside appraisal companies. Am. Compl. ¶ 286. *See Atari*  
 47 *Corp. v. Ernst & Whinney*, 981 F.2d 1025, 1031 (9th Cir. 1992) (applying California law to find it unreasonable to  
 48 continue to rely on financial statements after plaintiffs knew information to the contrary).

49  
 50 <sup>4</sup> California Corporations Code Section 25500 states, in relevant part: "Any person who willfully  
 51 participates in any act or transaction in violation of Section 25400 shall be liable to any other person who purchases  
 or sells any security at a price which was affected by such act or transaction for the damages sustained by the latter  
 as a result of such act or transaction."

1 failure to properly plead the Outside Director Defendants' intent to defraud via a knowingly false  
 2 statement under California Corporations Code Section 25500 with the particularity required  
 3 under Rule 9(b) as set forth *supra*, plaintiffs' California Corporations Code claims fail for the  
 4 independent reasons that the Outside Director Defendants are not alleged to have been sellers  
 5 under Section 25400 and that there is no private cause of action for indirect involvement in  
 6 alleged wrongful activity under Section 25403.  
 7  
 8  
 9  
 10  
 11

12  
 13 **A. The Outside Directors Are Not Alleged to Be Sellers**

14 Section 25400(d) applies to a defendant who is "a broker-dealer or other person selling or  
 15 offering for sale or purchasing or offering to purchase the security." As interpreted by California  
 16 courts, this restriction requires that a defendant have *personally* purchased or sold the security.  
 17 *Kamen*, 94 Cal. App. 4th at 199-200. *Kamen* dismissed an officer from liability because he made  
 18 false statements only after he sold his stock, and dismissed another who sold no stock—despite  
 19 the fact that the company executed a \$103.5 million convertible note offering during the relevant  
 20 time period. *See also Murphy v. BDO Seidman LLP*, 113 Cal. App. 4th 687, 705, 6 Cal. Rptr. 3d  
 21 770 (2003) (affirming *Kamen*'s limits and holding that accountants who made misstatements  
 22 were not liable under Section 25400 because they had not purchased or sold shares). Plaintiffs  
 23 do not allege that any of the Outside Director Defendants sold securities of the type the plaintiffs  
 24 purchased or were in any way involved in the sales process. Therefore, plaintiffs' cause of action  
 25 under Section 25400 (and Section 25500) must be dismissed.  
 26  
 27  
 28  
 29  
 30  
 31  
 32  
 33  
 34  
 35  
 36  
 37  
 38

39 **B. There is No Private Cause of Action Under Section 25403**

40 Plaintiffs also plead a violation of California Corporations Code Section 25403. Am.  
 41 Compl. ¶ 376. California Corporations Code Section 25403 forbids "knowingly provid[ing]  
 42 substantial assistance to another person in violation of any provision of the corporate securities  
 43 law." However, unlike Section 25400, Section 25403 does not have a corresponding private  
 44 right of action. *See Apollo Capital Fund, LLC v. Roth Capital Partners, LLC*, 158 Cal. App. 4th  
 45  
 46  
 47  
 48  
 49  
 50  
 51

1 226, 255, 70 Cal. Rptr. 3d 199 (2007). This cause of action must be dismissed against the  
2  
3 Outside Director Defendants because plaintiffs may not bring such a claim.  
4

5 **VI. CONCLUSION**

6  
7 For the reasons set forth above, the Outside Director Defendants respectfully request that  
8  
9 plaintiffs' claims against them in the Amended Complaint be dismissed with prejudice.  
10

11 DATED: February 16, 2010

**PERKINS COIE LLP**

12  
13  
14 By: s/Ronald L. Berenstein

15 Ronald L. Berenstein, WSBA #7573

16 David F. Taylor, WSBA #25689

17 Sean C. Knowles, WSBA #39893

18 1201 Third Avenue, Suite 4800

19 Seattle, WA 98101-3099

20 Phone: (206) 359-8000

21 Fax: (206) 359-9000

22 Email: [rberenstein@perkinscoie.com](mailto:rberenstein@perkinscoie.com)

23 [dftaylor@perkinscoie.com](mailto:dftaylor@perkinscoie.com)

24 [sknowles@perkinscoie.com](mailto:sknowles@perkinscoie.com)  
25  
26  
27  
28  
29

30 *Attorneys for Defendants Stephen E. Frank,*  
31 *Thomas C. Leppert, Phillip D. Matthews,*  
32 *Michael K. Murphy, William G. Reed, Jr. and*  
33 *Orin C. Smith*  
34  
35  
36  
37  
38  
39  
40  
41  
42  
43  
44  
45  
46  
47  
48  
49  
50  
51

**CERTIFICATE OF SERVICE**

I hereby certify that on February 16, 2010, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the email addresses indicated on the Court's Electronic Mail Notice List, and I hereby certify that I have mailed the foregoing document via United States first class mail, postage prepaid, to the non-CM/ECF participants indicated on the Court's Manual Notice List.

DATED at Seattle, Washington, this 16th day of February, 2010.

s/Ronald L. Berenstein

Ronald L. Berenstein, WSBA #7573

David F. Taylor, WSBA #25689

Sean C. Knowles, WSBA #39893

**PERKINS COIE LLP**

1201 Third Avenue, Suite 4800

Seattle, WA, 98101

Phone: (206) 359-8000

Fax: (206) 359-9000

Email: [rberenstein@perkinscoie.com](mailto:rberenstein@perkinscoie.com)

[dftaylor@perkinscoie.com](mailto:dftaylor@perkinscoie.com)

[sknowles@perkinscoie.com](mailto:sknowles@perkinscoie.com)

*Attorneys for Defendants Stephen E. Frank,  
Thomas C. Leppert, Phillip D. Matthews, Michael  
K. Murphy, William G. Reed, Jr. and Orin C.  
Smith*